

**From:** Pradipkumar Ramanlal  
**To:** Microsoft ATR  
**Date:** 1/28/02 10:58am  
**Subject:** Microsoft Settlement

This comment urges the presiding judge to reject the proposed settlement.

Little in the proposed settlement between "The Government" and "Microsoft" addresses one of the most perverse actions that Microsoft can take to

- (1) impede competition,
- (2) further strengthen its windows monopoly,
- (3) stifle innovation and
- (4) harm the consumer

The issue pertains to Microsoft's ability to bundle software. Microsoft has steadfastly maintained there should be (little or) no restriction on its ability to "innovate" (i.e., to add additional features to the Windows Operating System like Internet Explorer and Windows Media Player).

Unless the issue of bundling is adequately addressed in any settlement, the following scenario will almost certainly prevail:

-----  
Innovators generally have a strong interest to expend large amounts of resources (money and talent) to create middleware because of the huge market that exists and the potential for windfall profits if successful.

But innovators are cognizant of the fact that the risk-rewards structure is extreme: winner-take-all.

Innovators are also cognizant of the fact that there is a significant advantage to being first-to-market.

Thus success demands aggressive competition and a quick outlay of large amounts of resources.

It is just such innovation and tactics that brought about technologies of significant value to consumers: the browser (by Netscape) and the streaming audio/video (by Realnetworks).

In a competitive system, innovators are willing to take huge risks if the potential for huge rewards exists. But Microsoft, by using its monopoly power, has successfully decoupled the rewards from the risk. It has found a way to lay claim on the reward following its discovery, while assigning the costs associated with unearthing this discovery to the original innovator.

How is this possible?

A big part of the innovative process is to uncover the product or service consumers demand most. To that end, innovators expend valuable resources on inventing all kinds of products and services since initially it is unclear which one will "click" with consumers.

Microsoft has simply to sit back and let all the innovators in the market do their creative work and expend their resources. Once the dust has settled, and the winning product or service is revealed, Microsoft steps

in and creates a product to compete solely with this winning product. In a competitive system, such a strategy would be futile lacking the "first-to-market" advantage. But not so for an entrenched monopolist.

By bundling its competing version of the winning middleware to the operating system, Microsoft has the benefit of offering a winning product without having incurred the true expense incurred in uncovering this winning product, which is the sum of all the resources spent by all innovators in total in uncovering this product (most of them of course unsuccessfully).

Traditionally, Microsoft has bundled this winning software into the operating system so that consumers have the perception that they get it for free.

What is being done is that Microsoft garnishes the product from the innovator and passes it on to the consumer at no charge.

Why shouldn't the government be happy if the consumer gets something for nothing? First, it stifles further innovation since innovators now understanding there are no rewards to taking high risks. Second, with more and more winning middleware products added to the operating system, the Windows monopoly becomes further entrenched at a disproportionately low cost to Microsoft. Third, with all future innovators deterred from the market, consumers must rely solely on the innovative power of the monopolist.

Of course, there is the proposed remedy that Microsoft offer different versions of the operating system at different prices to afford the winning middleware innovator the opportunity to profit.

This remedy is vastly subject to manipulation by Microsoft because the costs and revenues are decoupled. Costs are determined by the cumulative labor expenses of the industry as a whole and the success likelihood of any one firm, while revenues are determined by whatever Microsoft sees fit to set the price differential between the two versions of the operating system, one with and the other without the middleware.

Proposed price differentials based on the length of code are also subject to manipulation given that Microsoft can make its base-version operating system any length it chooses.

There is also the issue of when the APIs are made available to the outside innovator and Microsoft internal developers for software upgrades of this winning middleware. They must be made available at the same time.

Of course, Microsoft is apt to claim in future, as it has in the past, that the added winning middleware is now an "integral" part of the operating system and therefore the playing field with respect to API disclosures will not be level.

The only remedy to ensure future innovation persists is if Microsoft competes on the same terms as all the other innovators in generating new and winning middleware.

In the least disruptive way to Microsoft, this can best be accomplished by requiring Microsoft to form a wholly owned subsidiary with whom Microsoft has a public and transparent arms-length relationship on the same terms offered to all competitors producing bona-fide competing middleware.

Sincerely,

Pradipkumar Ramanlal  
Associate Professor of Finance  
University of Central Flroida  
Orlando, Florida